Office-Supreme Court, U.S.
FILED
OCT 5 1961
JAMES R. BROWNING, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

No. 286

UNITED STATES OF AMERICA,
Appellant,

v.

DIEBOLD, INCORPORATED,
Appellee.

On Appeal from the United States District Court for the Southern District of Ohio

MOTION TO AFFIRM

ABE FORTAS
WILLIAM L. MCGOVERN
VICTOR H. KRAMER
1229 Nineteenth Street, N. W.
Washington 6, D. C.
Attorneys for Appellee

Of Counsel:

ARNOLD, FORTAS & PORTER
1229 Nineteenth Street, N. W.
Washington 6, D. C.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

INDEX

	Page
Question Presented	1
Statement	2
The acquisition	4
HHM's long-term financial background	4
The 1959 current position	5
Internal cash generation inadequate despite partial liquidations	6
The 1959 union contract	6
Operating losses	7
Badges of insolvency	7
(a) Repeated overdrafts	7
(b) Settling overdrafts through overdrafts	8
(c) Creation of fictitious balances through multiple deposits and withdrawals	8
(d) Heavy use of demand loans	9
(e) Slow payment of trade accounts	9
HHM's position at the time of the closing	10
Disclosures after the closing	11
Continued decline in business and continued cash needs	12
The so-called alternative purchasers	12
(a) Colonel T. C. Davis	12
(b) James H. Boyce	13
(c) Lovell Manufacturing Company	14
Argument	15
Conclusion	24

CITATIONS

CASES:

	Page
Associated Press v. United States, 326 U.S. 1 (1945)	17
Crown-Zellerbach Corp. v. FTC, 1961 Trade Cas., ¶70,038 (9th Cir.)	23
Erie Sand & Gravel Co. v. FTC, 291 F. 2d 279 (3d Cir. 1961)	23
Farm Journal, Inc., 53 F.T.C. 26 (1956)	23
International Salt Co. v. United States, 332 U.S. 392 (1947)	17
International Shoe Co. v. FTC, 280 U.S. 291 (1930)	1, 15, 18, 21, 23
Northern Pacific R. Co. v. United States, 356 U.S. 1 (1958)	17
Pillsbury Co., 1960-61 F.T.C. Cas., ¶29,277	23
United States v. Jerrold Electronics Corp., 187 F. Supp. 545 (E.D. Pa. 1960)	23
United States v. Maryland & Virginia Milk Producers Ass'n, 167 F. Supp. 799 (D.D.C. 1958)	23

OTHERS:

Clayton Act, 38 Stat. 730 (1914), as amended, 15 U.S.C. § 12 *et seq.*, § 7	1, 15
H. R. Rep. No. 1191, 81st Cong., 1st Sess. (1949)	16, 17
Sen. Rep. No. 1775, 81st Cong., 2d Sess. (1950)	16
MacLachlan, Bankruptcy (1956)	18
U. S. Department of Commerce Guides for Business Analysis and Profit Evaluation (1959)	19

INDEX

	Page
Question Presented	1
Statement	2
The acquisition	4
HHM's long-term financial background	4
The 1959 current position	5
Internal cash generation inadequate despite partial liquidations	6
The 1959 union contract	6
Operating losses	7
Badges of insolvency	7
(a) Repeated overdrafts	7
(b) Settling overdrafts through overdrafts	8
(c) Creation of fictitious balances through multiple deposits and withdrawals	8
(d) Heavy use of demand loans	9
(e) Slow payment of trade accounts	9
HHM's position at the time of the closing	10
Disclosures after the closing	11
Continued decline in business and continued cash needs	12
The so-called alternative purchasers	12
(a) Colonel T. C. Davis	12
(b) James H. Boyce	13
(c) Lovell Manufacturing Company	14
Argument	15
Conclusion	24

CITATIONS

CASES:

	Page
Associated Press v. United States, 326 U.S. 1 (1945)	17
Crown-Zellerbach Corp. v. FTC, 1961 Trade Cas., ¶70,038 (9th Cir.)	23
Erie Sand & Gravel Co. v. FTC, 291 F. 2d 279 (3d Cir. 1961)	23
Farm Journal, Inc., 53 F.T.C. 26 (1956)	23
International Salt Co. v. United States, 332 U.S. 392 (1947)	17
International Shoe Co. v. FTC, 280 U.S. 291 (1930)	1, 15, 18, 21, 23
Northern Pacific R. Co. v. United States, 356 U.S. 1 (1958)	17
Pillsbury Co., 1960-61 F.T.C. Cas., ¶29,277	23
United States v. Jerrold Electronics Corp., 187 F. Supp. 545 (E.D. Pa. 1960)	23
United States v. Maryland & Virginia Milk Producers Ass'n, 167 F. Supp. 799 (D.D.C. 1958)	23

OTHERS:

Clayton Act, 38 Stat. 730 (1914), as amended, 15 U.S.C. § 12 *et seq.*, § 7	1, 15
H. R. Rep. No. 1191, 81st Cong., 1st Sess. (1949)	16, 17
Sen. Rep. No. 1775, 81st Cong., 2d Sess. (1950)	16
MacLachlan, Bankruptcy (1956)	18
U. S. Department of Commerce Guides for Business Analysis and Profit Evaluation (1959)	19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

No. 286

UNITED STATES OF AMERICA,

Appellant,

v.

DIEBOLD, INCORPORATED,

Appellee.

MOTION TO AFFIRM

Appellee, pursuant to Rule 16 of the Revised Rules of this Court, moves that the judgment of the District Court be affirmed on the ground that the question on which the decision of the cause depends is so unsubstantial as not to warrant further argument.

* * *

QUESTION PRESENTED

Whether the undisputed facts supported the District Court's factual conclusion that Herring-Hall-Marvin Safe Company was so hopelessly insolvent at the time of its acquisition by appellee that the acquisition could not violate § 7 of the Clayton Act. *International Shoe Co.* v. *FTC*, 280 U.S. 291.

STATEMENT

This is an appeal from a judgment of the District Court for the Southern District of Ohio, in favor of appellee Diebold, Incorporated (Diebold), in a suit by the Government under § 7 of the Clayton Act, challenging Diebold's acquisition of the assets of Herring-Hall-Marvin Safe Company (HHM). Before trial of the Government's affirmative case,[1] the Court concluded, on the proofs of both parties submitted on Diebold's motion for summary judgment, that the acquisition did not violate § 7 because, at the time thereof, HHM was a "failing company."

The District Court found that there was no genuine issue as to any material fact, and concluded that at

---

[1] Appellant's claim (J.S. 15) that except for the "failing company" issue, Diebold's acquisition of HHM was a violation of the antitrust laws, is pure assertion. It was roundly denied in Diebold's answer, and no trial of the matter has been had. Neither is the Government's bland assertion (J.S. 4, 20), that Diebold and HHM were two of only three "dominant" companies engaged in producing for the relevant market, supported by proof. In the first place the definition of "relevant market" is a question of bewildering complexity here. Bank equipment is largely nondistinguishable from office equipment generally and the largest companies in the field, such as Remington-Rand and Shaw-Walker, manufacture a general line of safes and office equipment used by banks. An equally large portion of Diebold's annual business is general office equipment designed alike for insurance companies, municipal offices, factory offices and banks. (Koontz Dep., pp. 10-11, 13, 18-19, 34-36, and Aff. I, ¶32, 34-39; Mosler Dep., pp. 228-29). Diebold's position is that there are numerous companies producing for its market, many of them (like Remington-Rand) far larger than operations the size of HHM and Diebold. (Koontz Dep., p. 34, Aff. I, ¶36-41; Mosler Dep., pp. 230-45). But even if a long trial succeeded finally in winnowing out a small line of equipment suitable only for banks, to speak of Diebold or HHM as "dominant" companies in a small, highly specialized field dominated by gigantic financial institutions such as Chase Manhattan and Bank of America is to lose all sense of reality.

the time of its acquisition by Diebold, on September 11, 1959, and for at least nine months prior thereto, HHM was hopelessly insolvent and faced imminent receivership.

It found that because of its precarious financial condition, HHM could not long have survived as an independent competitor in its line of business. But for the sale to Diebold, concluded the Court, HHM would have been forced to liquidate its business in insolvency proceedings, with resultant heavy losses to employees, creditors, and stockholders. (Fdgs. 28, 31)[2]

With respect to certain other parties who at times had made overtures with respect to HHM, the Court found that "none of these overtures ever approached the concreteness of a firm offer or a firm price and no financial data or operating figures were supplied by HHM." It found that Diebold purchased on HHM's

---

[2] Since the record as filed in this Court by appellant is not paginated, references to the record herein are in the form of references to particular record documents. "Fdg." refers to the District Court's findings by number; "Robinson Aff. I" refers to Robinson's five-page affidavit, filed with the summary judgment motion in January, 1961, "Robinson Aff. II" refers to his four-page affidavit filed March 1, 1961, and "Robinson Aff. III" refers to his two-page affidavit filed the same day; "Lybrand Rep. #1" refers to the "Report on Review of Certain Accounts and Records as of Various Dates During 1959" of Lybrand, Ross Bros. & Montgomery; "Lybrand Rep. #2" refers to that firm's "Summary Schedules of Assets, Liabilities, Shareholders' Equity and Operations"; and "Lybrand Rep. #3" refers to that firm's "Comparison of Company Statistical Data with that of Industry", all three of which reports were exhibits to Robinson Aff. I; "Mosman Aff." refers to his affidavit executed January 5, 1961; while "Mosman Rep. Int." refers to his affidavit making response to appellant's Interrogatories, executed January 13, 1961; "Koontz Aff. I" refer to his affidavit of September 1, 1960, filed in opposition to appellant's motion for preliminary injunction; "Koontz Aff. II" refers to his affidavit filed with the motion for summary judgment. Other references are self-explanatory.

terms, in reliance on HHM's representations, without full access to HHM's books and records. It concluded that Diebold was the only *bona fide* prospective purchaser for HHM's business; that no one else ever made an actual offer for HHM; and that by reason of its precarious financial condition, HHM could not have achieved a sale to anyone else. (Fdg. 26, 29, 30, 31). Accordingly, it ruled that appellee was entitled to judgment as a matter of law, under the "failing company" doctrine of the *International Shoe* case.

Since this case turns on its own facts as they were developed before the District Court, we make a full statement of the undisputed basic facts relating to the failing-company issue, as presented to the Court below.

The acquisition.—On September 11, 1959, Diebold acquired the assets of HHM for $3,000,000. The acquisition resulted from an offer by Warren Mosman, President of HHM, of a quick cash sale of HHM's assets. (Fdgs. 1 & 2).

HHM's long-term financial background.—The financial background of HHM before the acquisition shows a pattern of a long-term expansion of sales, on a totally inadequate working capital base, followed by a two-year period of constriction in its business, with the last year featured by a desperate shortage of essential working capital to support the business' operations. From June, 1950, to the 1959 acquisition, HHM had been short of working capital, and down through 1958, HHM's balance sheets continuously reflected liabilities in excess of its tangible net worth. (Fdgs. 4 & 6; Mosman Aff., p. 2; Lybrand Rep. #3, Sched. 1). Its current ratio (relationship of its current assets to its current liabilities) averaged only approximately 1.5 for the years 1951 through 1959, in contrast with

an average of 2.7 during the same years for all manufacturers of fabricated metal products. (Fdg. 6; Lybrand Rep. #3, Scehd. 1). Against this backdrop of a continually "thin" current position, HHM's net sales rose from $5,023,270 in 1949, to $6,898,633 in 1954, and to $10,672,279 in 1957. (Singman Aff., Ex. 7; Mosman Aff., p. 1).

During the fifties, although the annual balance sheets and profit and loss statements of HHM purported to show a modest annual improvement in HHM's financial condition, these "book figures" failed completely to reflect the actual condition of the company. The books were made up in accordance with management policy. For example, the Treasurer of HHM was informed by Mosman in a "Personal and Confidential" memorandum on June 16, 1958, of the following "goals for June 30, 1958" (the end of the fiscal year): "I would like to show a net profit after taxes of at least $150,000" and "I would like to show a net worth of approximately $2,100,000." The Treasurer endorsed "O.K." on the memo, and as of June 30, 1958, the profit and loss statement showed a net profit after taxes of $188,814, and the balance sheet, a net worth of $2,126,502. (Fdg. 20; Robinson Aff. II, Ex. 4).

The 1959 current position.—By 1959, the company was falling substantially below its sales goals, and, in fact, net sales had shrunk by approximately $300,000 per year from the peak year of 1957 (Fdg. 7; Mosman Aff., pp. 1-2); and the shortage of working capital to which the company had been subject for years had become acute. In June, 1959, HHM's current position was such that its net quick asset ratio (the relationship between cash and government securities on the one hand and current liabilities on the other) had dropped to

.074. This means that HHM's cash and government securities, as of that month, amounted to only 7.4% of its *current* liabilities. The average figure for all companies in the fabricated metal products industry was 37%—five times HHM's figure. (Fdg. 6; Mosman Aff., p. 3; Lybrand Rep. #3, Sched. 2).

Internal cash generation inadequate despite partial liquidations.—This adverse net working capital position obtained despite the retention by HHM of substantially all of its earnings after taxes and of the proceeds, totaling close to a half million dollars, from periodic liquidations of productive assets. In 1954, the company had received and retained $150,000 in insurance proceeds resulting from the destruction by fire of the facilities of a subsidiary. In fiscal 1955, it sold a division for $100,000. In fiscal 1959, it had sold another division for $98,000, and a subsidiary for $130,000. (Fdg. 5; Mosman Aff., pp. 2-3). During this period, annual dividends paid in this fairly closely held corporation were less than $12,000, the last such being paid in the fiscal year commencing July 1, 1958.[3] (Singman Aff., Ex. 1-6).

The 1959 union contract.—In March of 1959, HHM's union presented HHM with demands for wage costs which were higher than those in the area or in the industry. Because of its extremely weak working-capital position the company could not stand a strike, and it finally accepted the union's terms. Before accepting these terms, Mosman gave serious consideration to liquidation. (Fdg. 15; Mosman Aff., pp. 3-4).

---

[3] Appellant's reference to "dividends of $2.00 a share" (J.S. 10) becomes a little more meaningful when it is understood that less than 6,000 shares of stock were outstanding during this period.

Operating losses.—In fiscal 1959, sales were falling by approximately $300,000 at an annual rate. During the same period, inventories built up by $262,000. (Fdg. 8; Lybrand Rep. #2, Sched. 1; Mosman Aff., pp. 1-3).

It was later revealed that, between July 1 and September 10, 1959, HHM had suffered operating losses of $206,953.51. (Fdg. 16; Robinson Aff. I, ¶5).

Badges of insolvency.—The company's desperate cash and working capital position gave rise to the following manifestations, which generally were not discovered by Diebold until after the purchase was closed:

(*a*) *Repeated overdrafts.*—The company had checks drawn and outstanding in excess of its actual balance on account at its principal depositary (The First National Bank and Trust Company of Hamilton) on 69 of the 114 working days between April 1, 1959 and the consummation of the sale on September 11, 1959. These overdrafts[4] ranged in amount from $104.51 to $78,394.58.[5] The company had total net overdrafts,

---

[4] Appellant suggests that it may be somewhat harsh to call HHM "overdrawn" since none of its checks actually were refused payment when presented—it simply had more checks drawn and outstanding than the money it had deposited with its banks would permit! (J.S. 17, n. 10). We submit that most reputable firms and individuals would consider this an overdraft. What HHM obviously was doing was writing overdrafts and trusting that there would be a sufficient "float" of incoming items deposited by it in time to cover them.

[5] HHM's bank balances reflected modest minimum monthly balances during 1959—as low as $13.82 in September. (Fdg. 13) These balances did not properly reflect its condition, because they failed to reflect the overdraft checks sent to creditors, not yet having cleared the bank, which gave it an overdrawn position on 60% of the working days between April 1 and September 11. The statements also did not reflect the inflation of bank balances created through the extraordinary procedure described in (*c*) below, page 8.

in amounts varying from $1,123.72 to $66,890.68, outstanding on *all* of its commercial bank accounts on 41 days during the same period. (Fdg. 9; Robinson Aff. I, ¶7, & Ex. 1).

(*b*) *Settling overdrafts through overdrafts.*—It was subsequently disclosed that on every pay day during the entire month of May, 1959, the regular payroll account of HHM in its principal depositary had payroll overdrafts outstanding in amounts ranging from $24,466.29 to $54,297.52. During at least half of this month, the overdrafts on the regular payroll account were subsequently reimbursed by overdrafts on the company's general account in the same bank. The general account itself was overdrawn in amounts ranging up to $116,809.86. During this period, the HHM accounts in all banks had net overdrafts outstanding against them in substantial amounts—as much as $79,037.17. (Fdg. 10; Robinson Aff. I, ¶8; Lybrand Rep. #1, Sched. C).

(*c*) *Creation of fictitious balances through multiple deposits and withdrawals*—The following extraordinary transaction was repeated on numerous distinct occasions. On January 30, 1959, HHM drew a check for $34,000 on a San Francisco bank for deposit in a New York bank; on the same day, a check for the same amount was drawn on the latter bank for deposit in a Pittsburgh bank; and on the same date, a check in the same amount was drawn on the Pittsburgh bank for deposit in HHM's Hamilton bank. Thus by the simultaneous transfer and retransfer of a single $34,000 deposit, on February 2, 1959, HHM was able to create a total aggregate balance of $136,000 in these four widely scattered banks. The same *modus operandi* (bearing striking resemblances to what is popularly

called "kiting") was followed by HHM on six other occasions in the first half of 1959. (Fdg. 13; Robinson Aff. II, ¶2 & 3)

(*d*) *Heavy use of demand loans.*—During the period in question, HHM borrowed money on a demand note basis from its principal bank depositary in Hamilton. The bank was limited by law from making loans in excess of $300,000 to any one customer. During 1959, the demand notes never fell below $250,000, and on two occasions, the amount was raised to the legal limit. The bank did not wish to carry this loan at the legal limit permanently, and if the bank had called upon HHM to pay off the demand notes, the bank President did not know where HHM could have obtained the money to do so,[6] and believed that, in fact, it would not have obtained the money. (Fdg. 14; Fitton Dep., pp. 100, 107-8, 125).

(*e*) *Slow payment of trade accounts.*—Another interesting source of financing by HHM during the period in question was the device of preparing and dating checks for its trade creditors at the time the invoices were approved, but of not releasing them until later. As a result, a lapse of between 30 and 120 days between preparation of a check and its issuance and cancellation by the bank was not unusual. In 1959,

---

[6] Curiously enough, appellant's analysis seems to view this extraordinary loan transaction as an indication of HHM's financial strength. (J.S. 11) Obviously, no company in sound financial health borrows heavily on *demand* notes except as a last resort because such notes subject it to the arbitrary "call" of the bank. HHM's obtaining of this loan, under the circumstances, indicated no ability to borrow on normal "term" paper the enormous additional sums that would have been necessary to enable it to meet its past-due and current obligations, not to mention to survive on its own power.

before the acquisition, at least 100 HHM checks per month cleared the bank over thirty days after the date of the check. An interesting example of this practice appears in the condition of HHM's account with Alcoa. The latter had declined HHM's request in December, 1958, that its "30 days net" credit terms be extended to 90 days. HHM then proceeded to effect the extension itself by holding up Alcoa's checks for periods of close to 90 days. (Fdg. 18; Robinson Aff. II, ¶4, & Exs. 2 & 3; Ziegler Dep., pp. 49-50).

HHM's position at the time of the closing.—By the time of the September 11 closing, HHM's net quick asset ratio had declined to .03—its cash and government securities were equivalent only to 3 per cent of its current liabilities. (Fdg. 6; Robinson Aff. II, ¶5). It had a nominal bank balance in its principal depositary of $13.92 at the start of September—and even then its checks in the amount of $113,000 were in the hands of its creditors. At the closing HHM declined to tender a check to Diebold in settlement of this bank account, on the ground that the account was actually overdrawn on account of outstanding checks. The overdraft in this account as of the day before the closing was $53,978.59. If against this deficit there be credited its smaller positive balances in other banks, HHM on the day before closing had a net overall deficit in all bank accounts in the amount of $35,596.61. (Fdgs. 3, 9; Robinson Aff.I, ¶3; Lybrand Rep. # 1, Sched. A).

As stated, it was later discovered that between the beginning of the 1960 fiscal year on July 1, 1959, and the closing, HHM had suffered operating losses of $206,953.51. (Fdg. 16; Robinson Aff. I, ¶5). As of the closing, it had accumulated past due trade bills payable, dating back prior to January, 1959, in the amount

of $244,127.68. In addition to these past due bills, at the closing, HHM also had currently due trade bills payable in the amount of $499,833.66. (Fdg. 17; Robinson Aff. I, ¶ 6; Lybrand Rep. # 1, Sched. E). Upon acquiring HHM, Diebold immediately commenced advancing cash to HHM, and within the next three weeks it had advanced a total of $500,000.00 to meet current and past due obligations of HHM. (Fdg. 19; Lybrand Rep. #1, Sched. F).

Disclosures after the closing.—In the period immediately after the acquisition, the facts concerning HHM's desperate financial condition came to light.[7] They had not been known to Diebold before the acquisition.[8] Diebold then caused audits to be made of HHM's finances, and an operations survey to be made by independent management consultants. The consultants' report indicated poor supervisory methods, unsound and obsolete design of tooling and equipment, and unsatisfactory labor application. The report concluded

---

[7] Appellant spends considerable space (J.S. 5-6, 12-13) in an effort to suggest that the raising of the failing-company issue was some kind of afterthought. This ignores the fact that at the time Diebold acquired HHM, Diebold was almost wholly ignorant of the facts concerning its finances. (See note 16, *infra*). Indeed, these facts came to light only after the closing occurred, and Diebold had taken possession of HHM. This was, of course, after the commencement of this litigation (which occurred over two weeks before the closing) and after the filing of many of the papers referred to by appellant.

[8] There is one minor exception. In May, 1959, Mosman told Diebold that, on the HHM April 30, 1959 interim balance sheet, he had reclassified $100,000 of receivables as cash. (Robinson Aff. I, ¶2). This was, as the statement of facts makes evident, hardly even chapter one in a complete financial story of HHM; and the proofs are clear that the rest of the HHM picture was learned by Diebold only after the closing. (See Fdgs. 16, 17, 18, 21, 29; Robinson Aff. I, ¶4-12; Koontz Aff. II, ¶1-2).

that HHM was a marginal operation. (Fdg. 21; Koontz Aff. II, ¶ 2).

Continued decline in business and continued cash needs.—After the acquisition, the pattern of losses continued, although, of course, now covered by Diebold's cash advances. Operations of the HHM Division of Diebold continued to reflect losses through the first seven months of 1960, culminating in a loss of $106,000 for the month of July, 1960. In the eight months ending August 31, 1960, new orders entered by the HHM Division declined $2,307,707, or 29.8 per cent, from the same eight-month period in 1959. Other indicators showed a continual decline in business. (Fdgs. 23 & 24; Koontz Aff. II, ¶ 4-5).

Cash advances, despite the shrinkage of the business, continued; by June 30, 1960, Diebold's cash advances to the HHM Division had been increased to $840,000. (Fdg. 19; Koontz Aff. II, ¶ 7). The decline in sales and shipments of the HHM Division required the continual lay-off of employees in HHM's main plant at Hamilton, Ohio. Employment at the Hamilton plant declined from 664 employees on September 11, 1959, to 370 on February 10, 1961, a total reduction of 294 employees, or approximately 45 per cent. (Fdg. 25; Robinson Aff. II, ¶ 6, and Ex. 1).

The so-called alternative purchasers.—Appellant has suggested that there were non-competing prospective purchasers who were "interested" in acquiring the business of HHM. (J.S. 13). Apparently, the references are to the following:

(*a*) *Colonel T. C. Davis.* One Van Ness, a New York bank employee, heard in the spring of 1959 that a certain Colonel T. C. Davis "might have some pos-

sible interest in trying to arrange an exchange of HHM stock for that of some company in which Colonel Davis had a present interest." Van Ness attempted to bring Mosman and Colonel Davis together. When contacted, "Colonel Davis indicated he had little knowledge of the HHM company, but that he was always willing to explore an investment possibility." Van Ness, after a few contacts with Mosman, and after informing Mosman that he could not predict whether negotiations with Davis held any promise, secured an expression of willingness from Mosman to meet Davis. Colonel Davis evidently then went on a European trip, and no meeting between the parties ever ensued. Notably, no "financial data or operating figures [were] ever supplied to Colonel Davis by Mr. Mosman." (Van Ness Aff., & Exs.).

(*b*) *James H. Boyce*—Mr. Boyce, of Baton Rouge, Louisiana, connected with various enterprises such as a Baton Rouge machinery sales and service company, a local Ford dealership, and an automobile leasing company, contacted Mosman in the middle of 1958, saw his plant in August 1958, and had sporadic contact with him for some time in 1959. In all this period, Boyce states that "a definite offer was never made" by him for the acquisition of HHM.

Boyce's Washington attorney attempted to promote a deal for HHM by soliciting Hayden, Stone & Co., New York investment bankers, circulating a pamphlet outlining a scheme for financing the deal. While this pamphlet was replete with estimates and projections of HHM's future earnings through 1968, Mosman had never made any disclosure of the real condition of HHM's finances to the promoters who prepared it. The solicitation stated that "it should be distinctly

understood that the following in no way constitutes an offer, but rather a basis for discussion," and indicated that the purchase would be made by a "purchasing group"—not yet formed—which might then float a public stock issue. The pamphlet was never brought to Mosman's attention, but Boyce orally mentioned, in discussions which never ripened into an offer, a plan contemplating debt financing in the sum of $1,500,000, or a long-term lease of HHM's fixed assets and outright acquisition only of the rest of the business.

During the period of about ten months during which the Boyce contacts took place, Boyce admits that "a definite offer was never made" by him for the acquisition of HHM. Mosman indicated that he was not interested in a sale for credit, which was always contemplated by Boyce. There was no evidence that Mosman made any financial disclosures to Boyce, of what effect an accurate disclosure of HHM's condition would have had upon Boyce, upon the "purchasing group" the pamphlet contemplated, or upon a prospective financer of the deal. (Boyce Aff., & Exs.; Mosman Rep. Int. 4, 5 & 6).

(*c*) *Lovell Manufacturing Company.*—Lovell Manufacturing Company of Erie, Pennsylvania, deals in clothes wringers and dryers. Representatives of Lovell and HHM had a meeting in April, 1959, at which Mosman mentioned a figure of $3,000,000 in cash. Lovell stated that they were not interested under such circumstances. After the meeting, Lovell wrote HHM, "You can expect to hear further from us within the next few weeks regarding some preliminary ideas concerning the matters which we discussed." Nothing of significance appears to have followed. (Mosman Rep. Int. 4, 5 & 6, & Exs.).

The District Court found that these three interests were but "promoters," who made no actual offer for HHM, that HHM's condition dictated that it make a quick sale without exhaustive analysis of its books and records, and that Diebold was the only *bona fide* prospective purchaser (Fdgs. 29, 30).

ARGUMENT

1. In *International Shoe Co.* v. *FTC*, 280 U.S. 291 (1930), the Supreme Court enunciated the following very practical doctrine:

> "In the light of the case thus disclosed of a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of a business failure with resulting loss to its stockholders and injury to the communities where its plants were operated, we hold that the purchase of its capital stock by a competitor (there being no other prospective purchaser), not with a purpose to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequences otherwise probable, is not in contemplation of law prejudicial to the public and does not substantially lessen competition or restrain commerce within the intent of the Clayton Act. To regard such a transaction as a violation of law . . . would 'seem a distempered view of purchase and result.'" (280 U.S., at 302-03).

This principle has ever since been styled the "failing company" doctrine. The establishment, on the facts of a given case, that the acquired firm was a "failing company" avoids a charge that its acquisition violates § 7 of the Clayton Act.

While the *International Shoe* decision was rendered under the original § 7 of the Clayton Act, the legislative history of the 1950 revision of § 7 makes it perfectly plain that Congress intended the doctrine to be available on the same terms under the Act as amended. The Senate Report declares:

> *"Companies in a failing or bankrupt condition:*
>
> "The argument has been made that the proposed bill, if passed, would have the effect of preventing a company which is in a *failing* or bankrupt condition from selling out.
>
> "The committee are in full accord with the proposition that any firm in such a condition should be free to dispose of its stock or assets. The committee, however, do not believe that the proposed bill will prevent sales of this type.
>
> "The judicial interpretation on this point goes back many years and is abundantly clear. According to decisions of the Supreme Court, the Clayton Act does not apply in bankruptcy or receivership cases. Moreover, the Court has held, with respect to this specific section, that *a company does not have to be actually in a state of bankruptcy to be exempt from its provisions; it is sufficient that it is heading in that direction with the probability that bankruptcy will ensue.*" (Quoting from *International Shoe*) (Sen. Rep. No. 1775, 81st Cong., 2d Sess. (1950), p. 7, emphasis supplied).

And the House Report:

> "The argument that a corporation in bankrupt or *failing* condition might not be allowed to *sell to a competitor* has already been disposed of by the courts. It is well settled that the Clayton Act does not apply in bankruptcy or receivership cases. In the . . . [*International Shoe* case] the

> Supreme Court went much further . . ." (quoting) (H.R. Rep. No. 1191, 81st Cong., 1st Sess. (1949), p. 6, emphasis supplied).

Appellant does not appear to dispute the validity of these principles. Neither does it clearly identify any principle of law concerning the failing-company doctrine which this Court might expound on the facts of the present case. Appellant's quarrel seems simply to be with the respective relevance of the various undisputed financial facts presented to the District Court in this case.[9]

2. The undisputed basic facts solidly establish that HHM was a "failing company", well within the *International Shoe* doctrine, at the time of its acquisition by Diebold. A picture was presented of a long-term shortage of working capital during the fifties against a pattern of overexpansion of the business. When business contracted after 1957, there was generated a desperate "current" position in HHM's finances, which came to a head during 1959. This was attended by accounting and financial practices on HHM's part which were not, to put the matter delicately, in the usual course of trade.

---

[9] Appellant raises, without arguing, the question whether the issues could properly be determined on motion for summary judgment. (J.S. 15). Where the basic facts are undisputed, as here, and where there is controversy only as to the inferences to be drawn from a mass of financial data, summary judgment would obviously be appropriate. Such a procedure was followed in *Associated Press* v. *United States*, 326 U.S. 1 (1945); *International Salt Co.* v. *United States*, 332 U.S. 392 (1947); and *Northern Pacific R. Co.* v. *United States*, 356 U.S. 1 (1958), where the grant of a Government motion for summary judgment in antitrust proceedings was affirmed by this Court.

During the period in question, immediately before and at the time of the acquisition, HHM was clearly insolvent in the "equity" or "commercial" sense,[10] —"the company had reached the point where it could no longer pay its debts as they became due." *International Shoe,* 280 U.S., at 300.[11]

HHM's failing condition had various badges. It arbitrarily held up the payment of its trade accounts. It wrote checks against the "float" in its accounts. It was overdrawn frequently. It engaged in transfers to create fictitious balances. Its quick asset ratio indicated utter distress throughout this period. By the time of the acquisition, net quick assets were down to 3% of current liabilities, and the company had heavy overdue trade bills.

The fact that HHM was a "failing company" during this period, and the merit of the application of the doctrine here, are confirmed by the enormous amounts of cash, which clearly HHM could not have raised itself, pumped into it by Diebold immediately after the acquisition. This is further buttressed by the continued operating losses that continued to affect HHM after the acquisition. Clearly, if there had been no acquisition, on the date, September 11, 1959, when HHM was acquired, HHM's days would have been numbered.

---

[10] This is the most common use of the term "insolvency". See MacLachlan, Bankruptcy (1956), § 13.

[11] This failure of a company through collapse of its current position during a time of business contraction was the very same type of business failure presented by the facts in *International Shoe*, in which the Court's conclusion was reached over a dissent which stressed the long-term prospects for the company. 280 U.S., at 306.

Appellant contends that the District Court reached its conclusion that HHM was a "failing company" on the basis of an "incomplete" picture of the company's "basic" financial position. (J.S. 4, 17). More simply stated, appellant is contending that the District Court erred in viewing as irrelevant and noncontrolling those details of HHM's finances which appellant submitted and relied on.

Appellant primarily objects to the District Court's conclusion that the long-term projections and historic balance sheet figures which it submitted were not controlling in view of the immediate financial crisis confronting HHM. But the financial crisis in which HHM found itself was not primarily related to its long-term prospects, but to its current position. The "long term" means nothing to a company which will not survive to enjoy it. The materials now stressed by appellant are simply not relevant to the central issue of fact—HHM's current position during the summer of 1959—on which decision in this case turned. If anything, the long-term figures offer an explanation of the background causes of the 1959 debacle—a long period of expansion, supported by inadequate working capital, followed by a cutback in sales, sudden, sharp increase of inventories, shortage of current funds, increased costs, and attendant insolvency.[12]

---

[12] "Somewhat more difficult to see are potential dangers that arise when a business has too great a turnover of its working capital, when too large a volume of business is being supported by its working capital. The business may be very profitable, further obscuring any danger. It should be emphasized that when sales are supported by an inadequate working capital, the very delicate balance of incoming and outgoing funds that results is easily upset with any interruption in the flow of funds, such as the sudden loss of sales or poor collection performance." U. S. Department of Commerce, Guides for Business Analysis and Profit Evaluation (1959), p. 17.

Thus, the fact, stressed by appellant (J.S. 9), that HHM's sales steadily increased from 1950 through 1957 scarcely militates against the District Court's conclusion that HHM was unable to pay its bills in 1959. The condition of its "retained earnings" account, its profit and loss account, or the other non-asset accounts [13] relied on by appellant (J.S. 9), bears no relation to HHM's current position in 1959. The "basic" element in HHM's financial picture was that it had no money to pay its bills. Bills must ultimately be paid out of money in the bank, not out of accounting charge accounts like "earned surplus" and "profit and loss".

Again, the fact that HHM's return on investment amounted to an abstractly impressive percentage in the fiscal year ending June 30, 1959 (J.S. 9-10) is hardly significant in the light of the undisputed facts of HHM's financial plight before the closing in September, 1959.[14] Obviously a return on investment will be high in percentage terms where severe undercapitalization exists—until operating losses commence, as they did in the months before the acquisition, and current conditions become desperate.

Finally, the Government economist's affidavit comparing HHM's income tax and census reports with those of other corporations, and drawing conclusions as to their share of the market, basic soundness over the preceding five years, and the like (J.S. 10-11) has

---

[13] Even if they be taken at face value, though made to order by the Treasurer on the President's request.

[14] Appellant's references to HHM's "effective use of its financial resources" (J.S. 10-11) are apparently simply to this high ratio between income and working capital during the period in which HHM was showing earnings.

no bearing on the practical current financial plight in which the company found itself in the summer of 1959. Old income tax reports, census reports, and the opinions of Government economists as to the "long view," with all due respect, are no substitute for cash in the bank to pay bills—and lack of the latter was HHM's problem.[15]

When all the facts are considered in perspective, it is clear that the District Court correctly concluded that the relevant, undisputed proofs established that HHM was a failing company in the relevant period in 1959, and hence within the *International Shoe* doctrine.[16] The financial details do not require further sifting in this Court.

3. Appellant suggests that this case might furnish an appropriate vehicle for this Court to respond to the

---

[15] Appellant has suggested that the payment of a substantial sum for HHM's assets is inconsistent with its status as a failing company. (J.S. 18) This notion, of course, overlooks the facts as to Diebold's ignorance of HHM's true condition. And it might here be recalled that in *International Shoe* itself, as stated, note 11, *supra*, the acquired company had some long-term prospects, and stock worth $9,460,000 was given for it. 280 U.S., at 306. The point is that "long-term" prospects are irrelevant in the face of an immediate receivership, where the company may not survive to the "long term".

[16] Appellant stresses (J.S. 13, 18) that Diebold made some contract revisions favorable to HHM and Mosman personally, during the period when HHM was "*in extremis*", prompted by attempts by Mosman to get out of the contract. Since Diebold was ignorant of HHM's true financial condition, this may reflect favorably on Mosman's skill in negotiations, but it has no relevance to the question of the actual financial condition of HHM. Diebold has never contended that it consciously acquired HHM as a failing company. Under *International Shoe*, it is enough that the "effect" of the acquisition be one "of mitigating seriously injurious consequences otherwise probable," 280 U.S., at 302, that is, that the acquisition prevents the failure of a company in fact failing.

speculations of the commentators regarding the effect of the presence of alternative "bidders" on the *International Shoe* doctrine.[17] (J.S. 19-20). But this case hardly furnishes the raw materials for such an endeavor. The term "bidders" scarcely fits the figures involved here. No firm offer ever was made by any of them. Neither is there any evidence that any of these interests or promoters who actually even saw Mosman would have had available, or could have attracted, sufficient resources to close a purchase within the time the circumstances demanded. As to their contacts with HHM, Colonel Davis never took steps even to have the meeting the bank employee had promoted for him; Boyce obviously was thinking in unrealistic terms, clearly never brought matters to a head, and admits never having made a firm offer during the protracted period during which he had contacts with HHM; and Lovell's contacts never were seriously pursued by it in terms of negotiations; it does not even appear that it ever mentioned a starting figure.

To forecast that any of these figures, styled "promoters" by the District Court, would—or could—have been receptive to a quick sale of the sort that was clearly necessary under the circumstances, to contemplate how HHM's properties could have served as the collateral for the debt financing inevitably contemplated by these interests, or to imagine what the effect would have been if anything resembling full disclosure had been made by Mosman, is obviously to enter into the realm of speculation. Here the District Court realized,

---

[17] Appellant's position appears to be merely that the existence of an alternative "prospective purchaser" or "bidder" would make the "failing company" doctrine only "not necessarily" available, and only that such an acquisition "may" be a violation. (J.S. 20).

as did the Court in *International Shoe*, that afterthought alternatives to the "outright sale," so clearly demanded under the circumstances, were matters where "one guess is as good as the other," and could be "dismissed as lying wholly within the realm of speculation." 280 U.S., at 301. No issue of law warranting further argument in this Court is tendered by these facts.

4. Finally, appellant, presumably in an effort to suggest that this case presents substantial issues which should occupy the time of this Court, catalogs a half-dozen § 7 cases in which the "failing company" doctrine was asserted by the defense (J.S. 21). The only lesson that can be derived from these decisions (none of which appellant claims to have enunciated any principle of law at variance with that applied below) is that the matter is one which turns on the particular facts of each case. Appellant's proclaimed fear of an undue broadening of the *International Shoe* doctrine by a pattern of factual adjudications should be more than allayed by the fact that, in the overwhelming majority of the cases it has listed [18]—including both the cases

---

[18] In *Crown-Zellerbach Corp.* v. *FTC*, 1961 Trade Cas., ¶70,038 (9th Cir.) and in *Erie Sand & Gravel Co.* v. *FTC*, 291 F. 2d 279 (3d Cir. 1961), Courts of Appeals affirmed, on their facts, factual determinations by the FTC holding "failing company" status not proved. In *Farm Journal, Inc.*, 53 F.T.C. 26 (1956), and *Pillsbury Co.*, 1960-61 F.T.C. Cas., ¶29,277, the FTC also rejected "failing company" assertions on the facts. In *United States* v. *Jerrold Electronics Corp.*, 187 F. Supp. 545, 565 n. 44 (E.D. Pa. 1960), *aff'd*, 81 S. Ct. 755 (1961), the District Court expressed doubt whether such a status had been made out but found it unnecessary to decide the question. Only in *United States* v. *Maryland & Virginia Milk Producers Ass'n*, 167 F. Supp. 799, 808-09 (D.D.C. 1958) was the existence of such a status found on the facts, and only as to some particulars of the charges. The Government's appeal in that case does not appear to have sought review of this particular finding. See 362 U.S. 458 (1960).

decided subsequently to the ruling below [19]—application of the doctrine was, on the facts presented, rejected.

CONCLUSION

The decision below represents the correct application of the settled doctrine of the *International Shoe* case to a set of undisputed basic facts. No question of law is raised, and the factual elements stressed by the appellant were duly considered and obviously do not detract from the conclusion reached by the District Court. Review in this Court of the District Court's findings concerning HHM's financial plight at the time of the acquisition patently is not attended by any public importance.

Accordingly, this motion to affirm should be granted.

Respectfully submitted,

ABE FORTAS
WILLIAM L. MCGOVERN
VICTOR H. KRAMER
1229 Nineteenth Street, N. W.
Washington 6, D. C.
Attorneys for Appellee

Of Counsel:

ARNOLD, FORTAS & PORTER
1229 Nineteenth Street, N. W.
Washington 6, D. C.

October 1961

---

[19] The *Crown-Zellerbach* and *Erie Sand & Gravel* cases.